IN THE HIGH COURT OF PUNJAB AND HARYANA AT CHANDIGARH

ITR No.50 of 1987
Date of decision:15.11.2006

The Commissioner of Income Tax,Amritsar

....Petitioner

versus

Smt.Pukhraj Wati Bubber, Amritsar

....Respondent

CORAM: HON'BLE MR. JUSTICE ADARSH KUMAR GOEL
HON'BLE MR. JUSTICE RAJESH BINDAL

Present: Dr. N.L.Sharda, Advocate, for the revenue.

JUDGMENT:

Following question of law has been referred for the opinion of this Court by the Income Tax Appellate Tribunal, Amritsar Bench, Amritsar, arising out of its order dated 25.6.1986 in ITA No.440(ASR)/ 1985, for the assessment year 1982-83:-

> "Whether on the facts and in the circumstances of the case, the Tribunal was right in confirming the order of the AAC for directing the ITO to allow deduction of Rs.2,64,795/-, embezzled by one Shri Kishore Hemani as trading loss for the assessment year 1985-86, without considering the fact that Shri Kishore Hemani was never an employee of the assessee?"

The assessee claimed deduction on account of embezzlement by Kishore Hemani, who was representative of the assessee for recovering the sale proceeds. The said Hemani collected the amount from the customers but did not pay the same to the assessee. The assessee lodged FIR on 29.1.1981, on the basis of which charge sheet was also filed in the court of competent jurisdiction by the investigating agency. The claim was disallowed by the Assessing Officer on the ground that the assessee failed to lead evidence that Hemani was authorised by the assessee to make collection. On appeal, the appellate authority allowed the claim of the

assessee for the following reasons:-

(i) Letter dated 1.8.1983 by the Inspector (Police) made it clear that there was no hope of any recovery;

(ii)Payments received by Hemani were encashed through two fictitious firms;

(iii)The embezzled amount was liable to be treated as trade loss for the assessment year 1985-86.

On appeal by the revenue, the Tribunal upheld the view taken by the appellate authority relying upon judgment of the Hon'ble Supreme Court in **Associated Banking Corporation of India Limited v. CIT, Bombay,** (1965) 56 ITR 1.

We have heard learned counsel for the revenue and perused the findings recorded.

The liability to tax is on profit or gains of business computed in accordance with Sections 30 to 43D of the Income Tax Act, 1961 (for short, 'the Act'). Though, there is no provision for allowing deduction of a trading loss on account of embezzlement, Section 37 of the Act provides for any expenditure for the purpose of business and there has to be nexus between the business operation and the loss. If loss was directly connected with the business operation and incidental to carrying on of business, the same has to be allowed as a deduction.

In **Badridas Daga v. CIT** (1958) 34 ITR 10 (SC), an agent of the assessee withdrew amount from bank and misappropriated the same. It was held that having regard to accepted commercial practice and trading principles, it could be held that loss arose out of carrying on of business and was incidental to it. Same principle was followed in **CIT v. Nainital Bank Limited,** (1965) 55 ITR 707(SC). In the said case, cash amount was stolen in a dacoity. In **Ramchandar Shivnarayan v. CIT, AP**, (1978) 111 ITR 263, after review of case-law on the point, it was held that loss on account of theft had to be treated as trading loss as it was directly connected with the business operation and was incidental to carrying on of business.

Following the law laid down in the above judgments, we are of the view that the Tribunal was justified in allowing deduction on account of embezzlement which was held to be incidental to the carrying on of the

business and since there was direct and proximate connection and nexus between the loss and the business operation of the assessee.

The question referred is thus, answered against the revenue and in favour of the assessee.

Reference is disposed of accordingly.

(Adarsh Kumar Goel)
Judge

November 15, 2006
'gs'

(Rajesh Bindal)
Judge